

## Revenue Ruling 79-388, 1979-2 CB 270

### Section 862.--Income from Sources without the United States

*26 CFR 1.862-1: Income specifically from sources without the United States.  
(Also Sections 861, 871, 1441; 1.861-4, 1.871-7, 1.1441-1.)*

#### **[IRS Headnote] Nonresident alien; income source; pension payments.--**

A nonresident alien received pension payments from a domestic employer's qualified noncontributory pension plan for services performed in prior years both within and without the U.S. The portion of each payment that is attributable to earnings of the pension plan and the portion attributable to the employer's contributions with respect to services rendered within the U.S. are income from sources within the U.S. for purposes of sections 871(a)(1)(A) and 1441(a) of the Code.

[Text]

#### ISSUES

(1) To what extent are the pension payments from a United States trust to a nonresident alien subject to Federal income and withholding taxes, under the facts below?

(2) What is the proper allocation of income between United States and foreign sources of pension payments received by a nonresident alien individual, under the circumstances described below?

#### FACTS

*A*, a nonresident alien individual, began employment with a foreign branch of domestic corporation *X* in the foreign country of which *A* was a citizen. Subsequently, *A* was transferred to *X*'s office in the United States and remained in such employment until retirement on December 31, 1978. During *A*'s employment in the United States, *A* remained a citizen of the foreign country and *A*'s status in the United States during such period was that of a resident alien individual. Immediately upon retirement *A* returned to the foreign country and *A*'s status changed to that of a nonresident alien individual. Pension payments from *X*'s retirement plan, which included credit for services performed by *A* for *X*'s foreign branch, commenced in January 1979.

While employed in *X*'s branch in the foreign country, *A* was a participant in the United States retirement plan that *X* established and contributed to for all employees of *X*. The retirement plan invested the contributions and received income from such investments.

*X*'s retirement plan is a noncontributory arrangement with respect to employees that qualifies, under section 401(a) of the Internal Revenue Code, as a self-administered trustee plan, and is exempt from taxation under section 501(a). Section 871(f), relating to an exclusion from gross income for amounts received from certain qualified pension plans, does not apply to any amounts received by *A* from *X*'s retirement plan.

#### LAW AND ANALYSIS

Section 871(a)(1)(A) of the Code imposes a tax of 30 percent of the amount received by a nonresident alien individual as, among other items, interest, dividends, salaries, wages, annuities, and other fixed or determinable annual or periodical gains, profits, and income, to the extent the amount so received is from sources within the United States and is not effectively connected with the conduct of a trade or business within the United States.

Section 871(f) of the Code provides an exclusion from gross income for amounts received as an annuity from certain qualified pension plans.

Section 861(a)(3) of the Code provides that compensation for labor or personal services performed in the United States shall be treated as income from sources within the United States and section 862(a)(3) provides that compensation for labor or personal services performed without the United States shall be treated as income from sources without the United States.

Section 1.861-4(a) of the Income Tax Regulations provides that gross income from sources within the United States includes compensation for labor or personal services performed in the United States regardless of the residence of the payer, the place where the contract for service was made, or the place of payment.

Section 1.861-4(b)(1)(i) of the regulations provides, with respect to taxable years beginning after December 31, 1975, that when labor or service is performed partly within and partly without the United States, the amount to be included in the gross income shall be determined on the basis that most correctly reflects the proper source of income under the facts and circumstances of the particular case.

Section 1.864-4(c)(6)(ii) of the regulations provides that pensions and retirement pay received by a nonresident alien individual attributable to personal services that constitute engaging in a trade or business in the United States constitute income that is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual if the individual is engaged in a trade or business in the United States at some time during the taxable year in which such income is received.

Section 1441(a) of the Code provides, in general, for the withholding of tax at a 30 percent rate on certain income from sources within the United States of nonresident alien individuals.

Section 1441(b) of the Code lists salaries, wages, annuities or other fixed or determinable periodical gains as items of income subject to the withholding of tax under section 1441(a).

Employer contributions to an annuity or pension plan represent compensation for personal services. *See* Rev. Rul. 56-82, 1956-1 C.B. 59. An employer's contributions to a pension plan with respect to wages earned abroad by a taxpayer is compensation for labor or personal services performed without the United States and are treated as derived from sources without the United States. *See* Rev. Rul. 72-149, 1972-1 C.B. 218.

*S. Rep. No. 1707*, 89th Cong., 2nd Sess. (1966), 1966-2 C.B. 1059 at 1077, relating to section 871(f) of the Code, states that, in cases to which 871(f) does not apply, a nonresident alien receiving pension income from a plan located in the United States is subject to United States tax on the interest portion of the pension income notwithstanding that employer contributions are wholly in respect of services performed abroad. *See also* Rev. Rul. 56-125, 1956-1 C.B. 627, which indicates that distributions to a citizen of the United States from a qualified pension trust are income from sources within the United States, to the extent such distributions represent earnings and accretions to contributions of either the employer or the employee.

## HOLDINGS

(1) Because *A* is a nonresident alien who is not engaged in a trade or business in the United States in 1979, the year *A* received the pension payments under consideration, the portion of the payments that is from United States sources is not effectively connected with the conduct of a trade or business within the United States and therefore is subject to the imposition of tax under section 871(a)(1)(A) of the Code, and to the withholding of tax under section 1441(a).

(2) (a) The part of each pension payment received by *A* from *X*'s United States pension plan that represents the earnings of the pension plan is income from sources within the United States.

(b) The part of each payment received by *A* under *X*'s plan that is attributable to *X*'s contributions with respect to services rendered by *A* outside the United States is income from foreign sources and the part received by *A* under *X*'s plan attributable to *X*'s contributions with respect to services rendered by *A* within the United States is income from sources within the United States.

For a related issue involving pension payments to a citizen of the United States, see Rev. Rul. 79-389, page 281, this Bulletin.